



CITY OF SANTA BARBARA

ORDINANCE COMMITTEE AGENDA REPORT

AGENDA DATE: April 1, 2008

TO: Ordinance Committee

FROM: Housing and Redevelopment Division, Community Development Department

SUBJECT: Inclusionary Housing Ordinance Revisions

RECOMMENDATION:

That the Ordinance Committee review possible revisions to the City's Inclusionary Housing Ordinance and forward a revised Ordinance to the City Council with recommendations.

EXECUTIVE SUMMARY:

Some Councilmembers and members of the public have expressed concern that the City's current Inclusionary Housing Ordinance ("Ordinance") does not adequately address the need for affordable (middle-income) housing in the City and does not go far enough in furthering the stated goals and purposes of the Ordinance. Council asked Housing Programs staff, the City's Housing Policy Steering Committee, and Planning Commission to review the Ordinance, consider appropriate revisions, and return to Council with recommendations.

In August, 2007, Council reviewed such recommendations and referred the matter to Ordinance Committee with direction to reject certain recommended changes and implement others, and to return to Council with a revised Ordinance for consideration and possible introduction/adoption. A five-member supermajority is required for amendment of the Ordinance, per City Charter Section 1507.

Council decided to defer consideration of some of the recommended changes until the discussion of revisions of the City's General Plan through the PlanSB process. More specifically, Council chose not to implement *at this time* the recommendations of the Housing Policy Steering Committee and the Planning Commission that the percentage of required inclusionary units be increased from 15% to 20% for some types of projects.

However, Council did request the Ordinance Committee to further explore the recommendation that the Ordinance be revised at this time to apply to projects of 2 or more units rather than the current minimum project size of 10 units. Council also requested the Ordinance Committee to consider various other possible revisions, such as the method of calculating the in-lieu fee and permitted uses of collected in-lieu fees. These possible revisions to the Inclusionary Housing Ordinance are the subject of this staff report.

REVIEWED BY: _____ Finance _____ Attorney

Agenda Item No. _____

BACKGROUND:

The City's Inclusionary Housing Ordinance was adopted in 2004. This Ordinance requires that all ownership subdivisions of 10 or more units, whether new construction or condominium conversions, are required to provide 15 percent of the total units as "inclusionary units." This requirement applies equally to residential zones and commercial zones. Inclusionary units must be sold at prices affordable to "middle-income" households which are households with incomes from 120% to 160% of the area median income. The current 2008 affordable sale prices for inclusionary units are \$249,900 for a 2-bedroom unit and \$283,300 for a 3-bedroom unit. Developers are entitled to a density bonus for each required inclusionary unit. Projects such as apartments that may not be sold separately are exempt from the Ordinance.

Purpose and Intent: The Ordinance incorporates a number of findings that indicate its purpose and intent. These include the following (edited for brevity):

- A lack of new inclusionary housing units will have substantial negative impacts because, without more affordable housing close to employment centers, commutes will increase, traffic will worsen, and City businesses will find it more difficult to attract and retain the workers they need.
- Development of new market rate housing (and conversion of apartments to condominiums) encourages new residents to move to the City. This increases the demand for new services, and the service providers who are in the middle income category cannot afford to buy homes here. These employees may feel forced to commute long distances.
- Santa Barbara has very effective affordable housing programs, but 90 percent of the City's affordable housing is *rental* housing for very-low and low income residents. There is an increased need to create home ownership opportunities for middle income (and upper-middle income) households, but federal and state subsidy funds are not available for these income categories.

Are Goals Being Met as Fully as Possible? Some Councilmembers and members of the public have expressed concern that the current Ordinance does not go far enough in furthering its stated goals and purposes. For example, should the Ordinance be amended to apply to smaller projects than it currently does?

Threshold Number of Units: The current Ordinance does not apply to projects smaller than 10 units. But the majority of ownership housing projects, both new construction and condominium conversions, have fewer than 10 units. Dozens of new ownership projects and condominium conversions with between 2 and 9 units have been approved in the 4 years since the Ordinance was adopted. Many more are currently in the development review process. The pace of apartment-to-condominium conversions with fewer than 10 units seems to be increasing. The current Ordinance does nothing to help mitigate the impact of these projects on the demand for affordable middle income housing.

The Ordinance findings summarized above state that new ownership housing increases demand for services provided by people who cannot afford housing in the City. These findings are just as true for new housing projects and condo conversions with fewer than 10 units.

DISCUSSION:

Recommendations of the Housing Policy Steering Committee and Planning Commission:

Council asked the City's Housing Policy Steering Committee ("Steering Committee") to review and make recommendations about possible revisions to the Ordinance. The Steering Committee met on this matter on April 10, 2007, for two hours and again on May 24, 2007, for three hours, heard input from members of the public, and made recommendations to the Planning Commission and Council about Ordinance revisions.

The matter then went to the Planning Commission, which held a noticed public hearing on changes to the Ordinance on June 21, 2007.

The majority of the Steering Committee members and Planning Commission members recommended that Council adopt the following revisions to the Ordinance:

1. Lower the Threshold: The threshold project size to which the Ordinance applies should be lowered from 10 units to 2 units. A lower inclusionary percentage would apply to these smaller projects. Projects of 2, 3 or 4 units would be subject to a 5% inclusionary requirement which could be satisfied by payment of a pro-rated in-lieu fee. Projects of 5 through 9 units would be subject to a 10% inclusionary requirement which could be satisfied either by payment of a pro-rated in-lieu fee or by building an affordable inclusionary unit on site. As with the current Ordinance, any required inclusionary unit would be entitled to a density bonus.

2. Increase the Inclusionary Percentages for Some Projects: With the cooperation and input of several local developers, staff developed detailed financial models to study impact of an increased inclusionary requirement on the financial feasibility of various projects. These financial models showed that reduced parking requirements inside the Central Business District (CBD) would enable projects to remain financially feasible with higher percentages of affordable inclusionary units. The models also showed that larger projects (over 25 units) benefited from economies of scale that also enabled these projects to remain financially feasible with higher percentages of affordable inclusionary units.

The Steering Committee and Planning Commission considered the financial models and heard input from developers and interested citizens. They recommended that Council adopt different inclusionary requirement percentages for various project sizes and locations. The current 15% requirement would remain for some projects (those with 10 to 24 units outside the CBD), but would be increased to 20% for other projects. Please refer to the following table for a summary of the recommendations, including the percentages for projects with fewer than 10 units:

Table 1

Inclusionary Percentages Recommended by the Steering Committee and Planning Commission			
# of Units in the Project	Projects Outside the Central Business District	Projects Inside the Central Business District	Density Bonus ("by Right") for Required Inclusionary Units?
2 – 4	5%	7.5%	No
5 – 9	10%	15%	Yes
10 – 24	15%	20%	Yes
25+	20%	20%	Yes

Council Direction to Ordinance Committee:

On August 14, 2007, Council considered the recommendations of the Steering Committee and Planning Commission. The majority of the Councilmembers decided not to increase the inclusionary percentage above the current requirement of 15% at this time. Some Councilmembers thought that this change should be included in the PlanSB process for the update to the City's General Plan. Council chose not to make a distinction between projects inside the CBD and those outside.

The majority of the Councilmembers supported lowering the project size threshold from 10 units to 2 units at this time. The following table shows the changes to the inclusionary percentages that Council has forwarded to the Ordinance Committee.

Table 2

# of Units in the Project	Inclusionary Percentage	Density Bonus ("by Right") for Required Inclusionary Units?
2 – 4	5%	No
5 – 9	10%	Yes
10 and more	15%	Yes

Council also referred a few other remaining issues to the Ordinance Committee for consideration. These issues included the method of calculating the in-lieu fee and expanding the allowed uses of collected in-lieu fees.

Staff Recommendations to Ordinance Committee:

During the time that has passed since Council's referral to the Ordinance Committee, staff has come to believe that changes to the Ordinance that will result in an increase in the number of housing units in the City should be included in the PlanSB process for the update to the City's General Plan. The reason for this is that staff feels that the possible environmental impacts from any additional units generated by revisions to the Ordinance would best be assessed as part of the environmental review of the General Plan update. The revisions that will be proposed to the General Plan will undoubtedly have some effect on the "build-out" potential of the City (i.e. the number of additional units that will be allowed under the zoning ordinance and General Plan). The environmental impact of this change will be the subject of a comprehensive (and costly) EIR. It would be more efficient to include the more significant revisions of the Ordinance (if any are endorsed by Council through the PlanSB process) as part of that environmental review. It is true that this approach will delay the implementation of more significant changes to the Ordinance, but staff feels that the delay is justified by the added integration and efficiency of the environmental review. This approach is consistent with the stated preference of some Councilmembers to similarly postpone the consideration of increase in the inclusionary percentage for 15% to 20% for some projects.

In order to assure that the current recommended changes to the Ordinance would not result in additional units (due to entitlement to additional density bonus units), staff is now recommending that the inclusionary percentage for projects of 5 through 9 units be set at 5%, rather than 10%.

With the 10% inclusionary requirement that had been recommended, projects of 5 through 9 units would be required to provide an inclusionary unit (10% of 5 units = 0.5 units, which would be rounded up to one full unit. As an alternative to providing the unit on-site, the developer could choose to pay a pro-rated in-lieu fee. The pro-rated fee would be 50% of a full in-lieu fee for a 5-unit project or 90% of the fee for a 9-unit project. If the developer chose to build an inclusionary unit on-site rather than pay the pro-rated fee, the developer would be entitled to a *density bonus* for that unit.

Instead, with a 5% inclusionary requirement, a 9-unit project would be required to provide less than one-half of an inclusionary unit (5% of 9 units = 0.45 units). This requirement would be satisfied by paying 45% of the in-lieu fee for 1 unit. There would be no requirement to build a unit on-site, and therefore there would be no entitlement to density bonus for an inclusionary unit. Thus, the revisions to the Ordinance proposed at this time would *not* result in an increase in the number of housing units in the City.

With this change, the staff recommendations to the Ordinance Committee are as follows:

1. Revise the Percentage Requirement for Smaller Projects (2 through 9 units): The following table shows the staff-recommended inclusionary requirement percentages for various project sizes.

Table 3

# of Units in the Project	Inclusionary Percentage	Density Bonus ("by Right") for Required Inclusionary Units?
2 – 9	5%	NA (none required)
10 and more	15%	Yes

2. Change the Method of Calculating the In-Lieu Fee: Staff recommends that the in-lieu fee calculation be modified slightly. When the Ordinance was adopted in 2004, the amount of the in-lieu fee was \$310,000, based on the formula in the Ordinance. Since then, the fee has increased to \$473,300 (over 50 percent higher). This increase is largely due to the increase in the median sale price of condos in the City (from \$500,000 to \$650,000). Staff is concerned that the fee has increased to the point that it is no longer reasonable.

Staff recommends a one-word amendment to the Ordinance that would bring the fee more in-line with the amount of the fee at the time the Ordinance was adopted. Currently the fee is calculated as the difference between the development cost of a 2-bedroom condominium in the City and the maximum sale price of a *low-income* affordable unit. Staff recommends that the words "low-income" be changed to "*moderate-income*." This revision would result in an in-lieu fee of \$354,000, as shown in the following table.

Table 4

	In-Lieu Fee Calculations	
	LOW (current)	MODERATE (proposed)
Median Sale Price of Condo in SB	\$650,000	\$650,000
Cost to Build (=85% of Sale Price)	\$552,500	\$552,500
Minus the Affordable Sale Price of a Low Income Unit:	(\$79,200)	NA
Minus the Affordable Sale Price of a Moderate Income Unit:	NA	(\$198,500)
In-Lieu Fee	\$473,300	\$354,000

Changing the Ordinance language from "low income" to "moderate income" would be consistent with the stated purpose of the Ordinance to create affordable ownership housing for moderate and above-moderate income households.

The revised in-lieu fee of \$354,000 for each required inclusionary unit would be pro-rated for fractions of a required unit. The 5% inclusionary requirement for projects of 2 through 9 units results in a fee of \$17,700 per unit. Thus, the in-lieu fee required of projects for 2 through 9 units would be pro-rated as follows:

Table 5

Number of Units	Times 5%	In-Lieu Fee
2	10%	\$34,500
3	15%	\$53,100
4	20%	\$70,800
5	25%	\$88,500
6	30%	\$106,200
7	35%	\$123,900
8	40%	\$141,600
9	45%	\$159,300

3. Expand the permissible uses of collected in-lieu fees. The current Ordinance states that collected in-lieu fees may be used for the development or rehabilitation of housing affordable to very-low, low and moderate income households. Staff strongly recommends that the Ordinance be revised to expand the allowable uses for collected in-lieu fees to include the following:

- The City's purchase and resale of middle and upper middle income affordable units that are in default in order to preserve the long-term affordability of such units. The fund would then be reimbursed upon the resale of the units to eligible households. This is a *crucial* allowable use for collected in-lieu fees, because the City's affordable housing subsidy funds (such as Redevelopment Agency housing funds and federal HOME funds) may not be used for above-moderate income housing, even for a short term purchase and resale.
- For the City to subsidize the creation of affordable middle and upper-middle housing. For example, in the future, the City may wish to assist a non-profit developer in building new affordable condo units for locally-employed middle and upper-middle income workers. None of the City's sources of affordable housing subsidy funds may be used for above-moderate income housing. In-lieu fees would be the only source for subsidies at middle and upper-middle income levels.
- Finally, allowing a portion of such funds to be spent on the City's administrative costs of monitoring and enforcing the compliance of inclusionary units with the City's affordable housing policies. Staff monitors each affordable unit annually as well as upon the initial sale, refinancings and re-sale. Again, *these in-lieu fees would be the only available source* for this important purpose, other than scarce City general funds.

4. Incorporate Miscellaneous Other Revisions: Staff recommends that the Ordinance Committee consider other minor changes to the current Ordinance as the Committee deems appropriate. These may include the following:

- Delay the payment due date for in-lieu fees for projects of 2 through 4 units until “prior to occupancy” rather than “prior to the building permit” in order to lessen the financial impact on these small projects.
- Eliminate the need for a lot-area modification for the inclusionary units that receive a density bonus by entitlement.
- In projects that include housing that is affordable to upper-middle income households per the City’s policies, exempt such affordable units from the inclusionary requirement. For example, an employer may sponsor a housing project that is 100% affordable to upper-middle income households (or below), and such a project would have no inclusionary requirement.
- Allow the Community Development Director some flexibility in setting the minimum number of bedrooms in the inclusionary units. The current Ordinance requires that average number of bedrooms in the inclusionary units must equal or exceed the average number of bedrooms in the market rate units. This may result in some rather harsh requirements in practice.
- Other minor changes deemed appropriate by the Ordinance Committee and subsequently by Council.

CONCLUSION:

The Ordinance Committee is requested to review the recommended changes, hear comments from interested members of the public, and direct staff to draft appropriate revisions to the Ordinance. Staff will return with a draft revised Ordinance at a subsequent meeting of the Ordinance Committee and request that the Committee forward it to Council. Adoption would require approval by a five-member supermajority of the Council.

PREPARED BY: Brian Bosse, Acting Housing and Redevelopment Manager/SBF

SUBMITTED BY: David Gustafson, Acting Community Development Director

APPROVED BY: City Administrator's Office